As every distributor is aware, mergers and acquisitions are gripping the industry as never before. In fact, a report conducted by Arthur Andersen & Co. speculated that the number of wholesale-distribution firms will decline 25% from 1987 to 1995.

While this figure is alarmingly high, ID's own numbers are consistent with those of the study. When distributors were asked whether they were approached with an acquisition offer during 1987, 30% indicated "yes." However, the *Survey* reveals that large distributors were approached nearly three times as often as smaller distributors.

In measuring both general line and specialty distributors together, only 16% of those with sales of $1 million or less reported being approached by an acquirer. But as sales increased, so did interest in the company. For example: 26% of distributors with $1 million to $2 million in sales were approached; $2.1 million to $5 million (44%); and $5 million-plus in sales (42%).

Of those looking to acquire, only 3% of the "million-dollar" distributors were actively seeking an acquisition, while 18% of those with "$5+ million" in sales were looking to acquire.

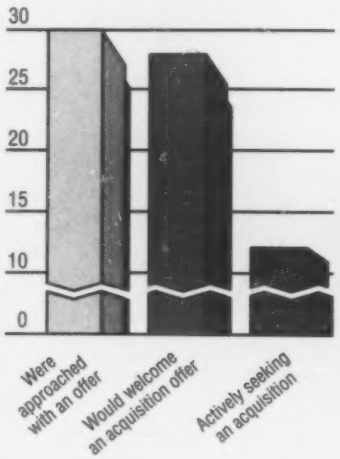
Other opinions expressed by management involved relationships with suppliers and customers. While 44% of distributors thought they would increase number of vendors in the next 2 years, again there was a decided difference when measured by sales.

In the "million-dollar" category, only 4% of distributors thought they would decrease their supplier bases; 31% of the largest distributors agreed. However, 88% of generalists and 92% of specialists speculated they would increase customer bases in the next 2 years. Only 81% of the smallest distributors thought that was likely, while 92% of the largest distributors expect to increase customer bases.

Survey methodology

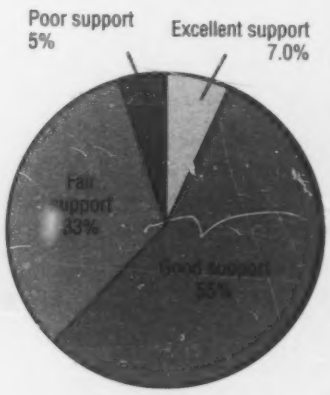
The *Survey* is actually two separate reports. The first was mailed to the headquarters of general line and specialist distributors, and is based on 307 returns. The second was mailed to combination houses, companies dividing their business between industrial and non-industrial markets; 119 companies participated. Margin of error is ±5%.

Acquisitions

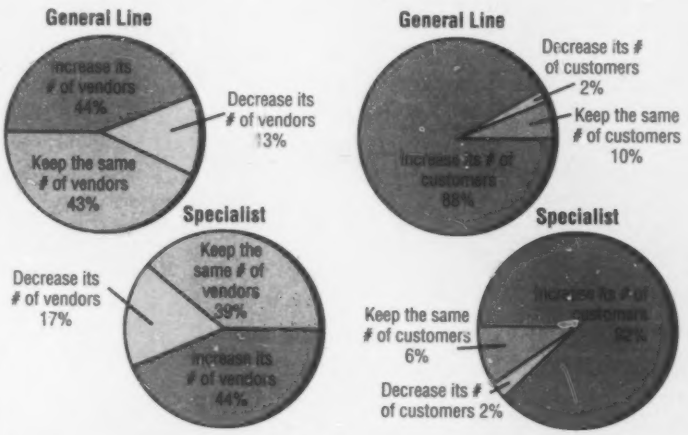


Vendor Support

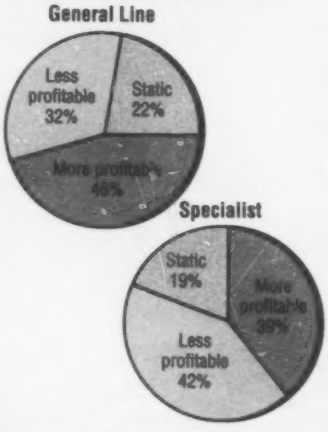
(In general, most vendors provide...)



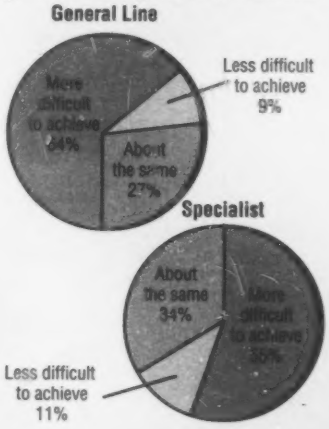
During the next 2 years, our company will...


General Line
Increase its # of vendors 44%
Decrease its # of vendors 13%
Keep the same # of vendors 43%
Specialist
Decrease its # of vendors 17%
Keep the same # of vendors 39%
Increase its # of vendors 44%
General Line
Decrease its # of customers 2%
Keep the same # of customers 10%
Increase its # of customers 88%
Specialist
Keep the same # of customers 6%
Decrease its # of customers 2%

In the past 5 years, distribution has become...



During the next 5 years, profit margins will be...



When it came to measuring inventory values, distributors showed little preference for method. Half indicated a preference for last-in-first-out (LIFO); only 40% of general liners value inventories by the first-in-first-out (FIFO) method.

In 1987, the average LIFO value for all distributors increased 8% to $230,000 while LIFO reserves soared 19%. In contrast, FIFO values during 1987 decreased nearly 9% to $331,000.

When the average monthly inventory values of companies using the LIFO method were examined, distributors with annual sales of $1 million or less were found to have increased LIFO values 40%: from $43,000 to $61,000. On the opposite side of the spectrum, distributors with $10 million-plus in sales increased LIFO values 11%.

Back in September '87, the American Production and Inventory Control Society (APICS) cautioned that inventory-to-sales ratios were "getting out of hand again" (**ID**: Nov. '87, p.39). Unfortunately, it appears that some distributors may have lost profits based on expectations that higher inflation would increase inventory profits. On the surface, at least, large distributors maintained a more cautious position and ultimately outperformed their smaller counterparts with 10.5% ROI versus 7%.

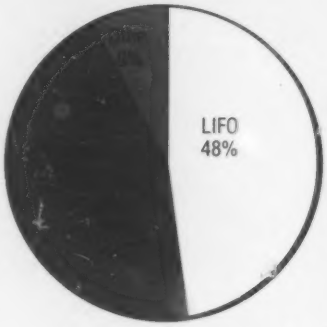
Other differences were not as dramatic. Neither general line nor specialty distributors managed to improve on collection efforts, although receivables for specialists were 45 days outstanding as compared to 41 days for generalists.

When it came to inventory turns,* large distributors once again capitalized on economies of scale. Distributors with sales of $10 million or less averaged 4 stock turns per year; the giants reported 7 turns per year.

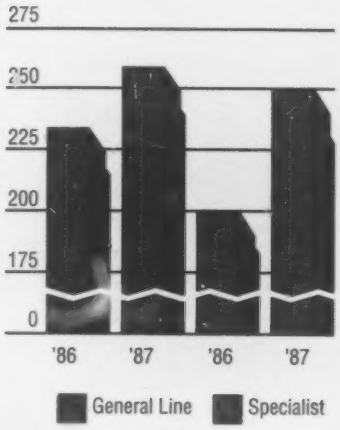
However, in yearly comparisons, neither general line nor specialty distributors improved their stock turns from 1986 to 1987, although general liners fared slightly better than specialists. One explanation for the difference is that specialists are more dependent upon value-added services for their sales than are generalists. In fact, generalists indicated that fully 65% of their sales are from stock on hand, while specialists claimed only 50%.

*Stock turns were calculated by multiplying the percent of shelf stock sales at cost by total sales and dividing the result by the average monthly inventory value.

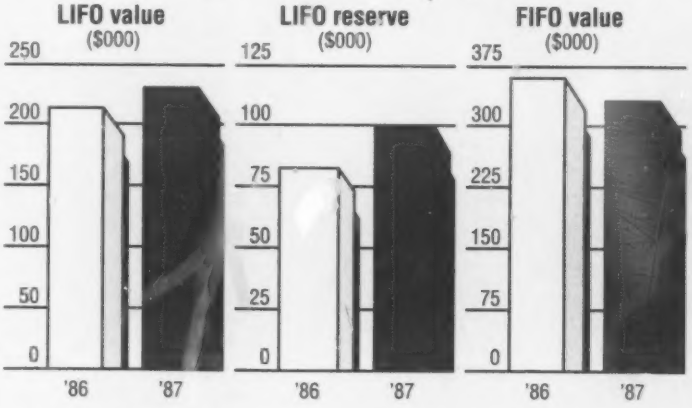
By what method do you value your inventory?



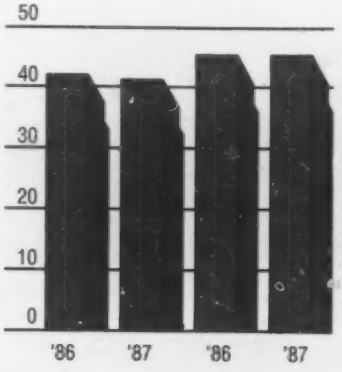
Receivables
(Year-end value $000)



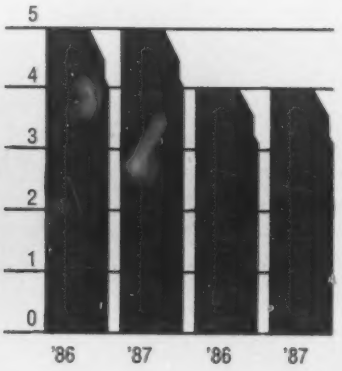
Average monthly inventory value



Collections
(Receivables outstanding in days)



Stock turns



PERSONNEL

The 1987 *Survey* revealed few clearly discernible trends in either new hirings or personnel deployment. Although the median average number of full-time employees increased from 10 to 11, such a difference is statistically too slight to confirm an overall direction. Further, there are no apparent changes in the placement of outside salespeople, inside (and telemarketing) salespeople, or counter salespeople.

During 1987 the average general line distributor employed 10 people, as opposed to 11 in 1986. Based on numbers obtained from the 1986 *Survey* as well as this year's report, specialists have resisted hiring new personnel since 1985, in spite of rising sales.

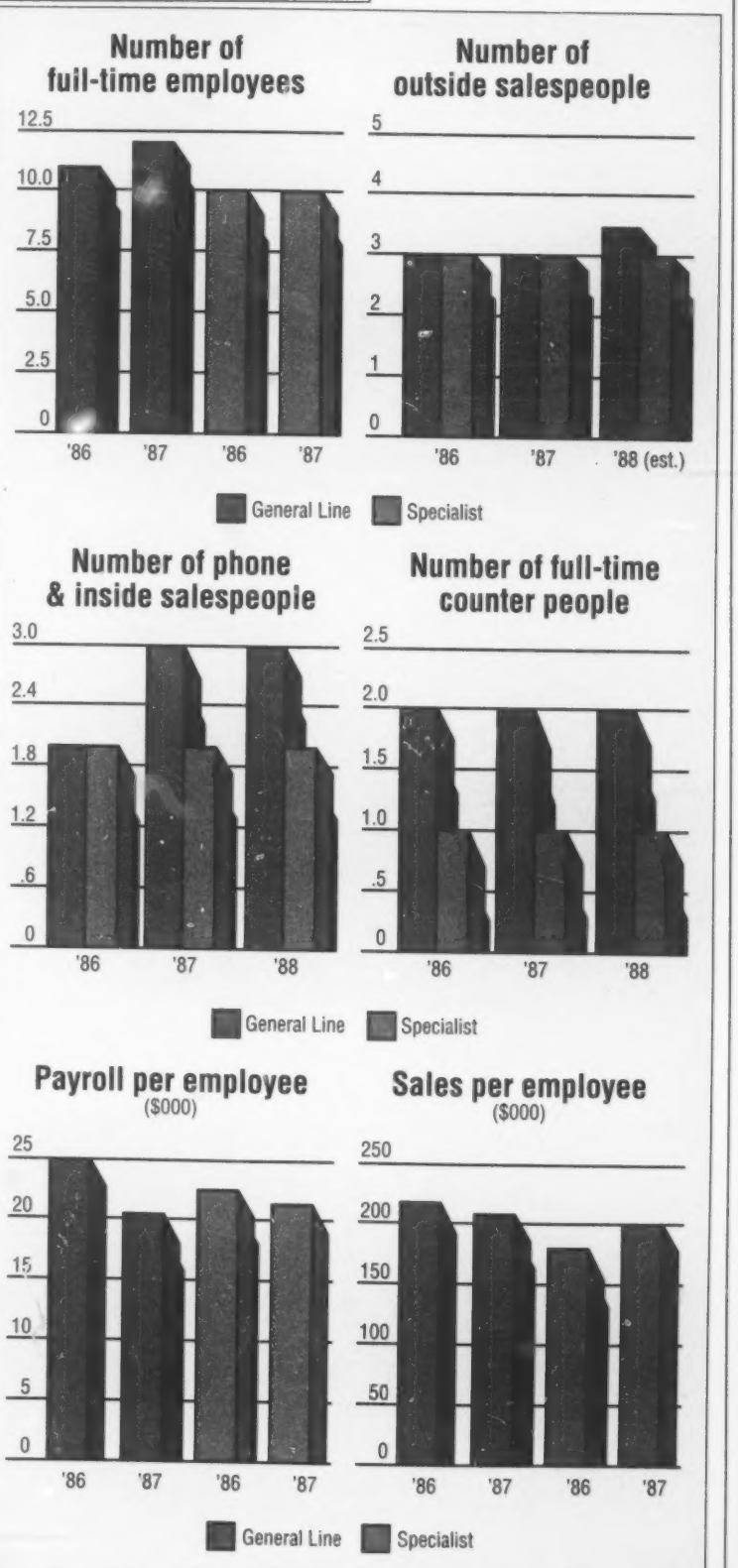
While most distributorships are in desperate need of experienced sales help, the prospects for those entering the field without job-related experience appears slight for the remainder of the year. When respondents to the questionnaire were asked to estimate hirings for 1988, demand for inside and telemarketing positions were the only category thought to increase. The hiring of outside salespeople and full-time counter salespeople is expected to remain unchanged.

What the *Survey* did discover, however, is that while general line distributors managed to eke out slightly greater sales per employee than specialists, should current trends continue, specialists will vastly outperform generalists in 1988.

Between 1986 and 1987, specialists increased their sales-to-employee ratios 11%, while generalists lost nearly 5% of their output. Although such measures are not a clear indicator of productivity, as both businesses are similar, large shifts sustained over several years may prove to be an important barometer.

Medians and averages

Unless otherwise noted, most percentages expressed in this report are median averages which, in their simplest form, define the midpoint in a statistical range (half of a group will be larger and the other half smaller than the midpoint). Medians are more representative of a group and are less distorted by extremes. Responses to open-ended questions are expressed in medians. Averages have been used to measure responses to closed-ended questions such as "yes" and "no."



WAREHOUSING

Although most distributors anticipate increasing both their customer and supplier bases, only 18% think it necessary to either enlarge their warehouse space or increase their number of stocking locations.

In measuring sales per square foot of warehouse space, specialty distributors managed to make more money with less available room. Averaging 5,000 square feet of warehouse space, specialists increased their sales-to-space ratio 11% to $400. On the other hand, the generalist averages an 8,000-square-foot warehouse and only managed a sales-to-space ratio of $313, an increase of 4.3% from 1986.

As was indicated earlier in this *Survey*, ratios can be misleading, particularly when two similar (but not identical) entities are being compared. What remains important are trends and, as has been seen throughout this report, the ability of the specialty distributor to continually outperform the general liner by virtually every important measure.

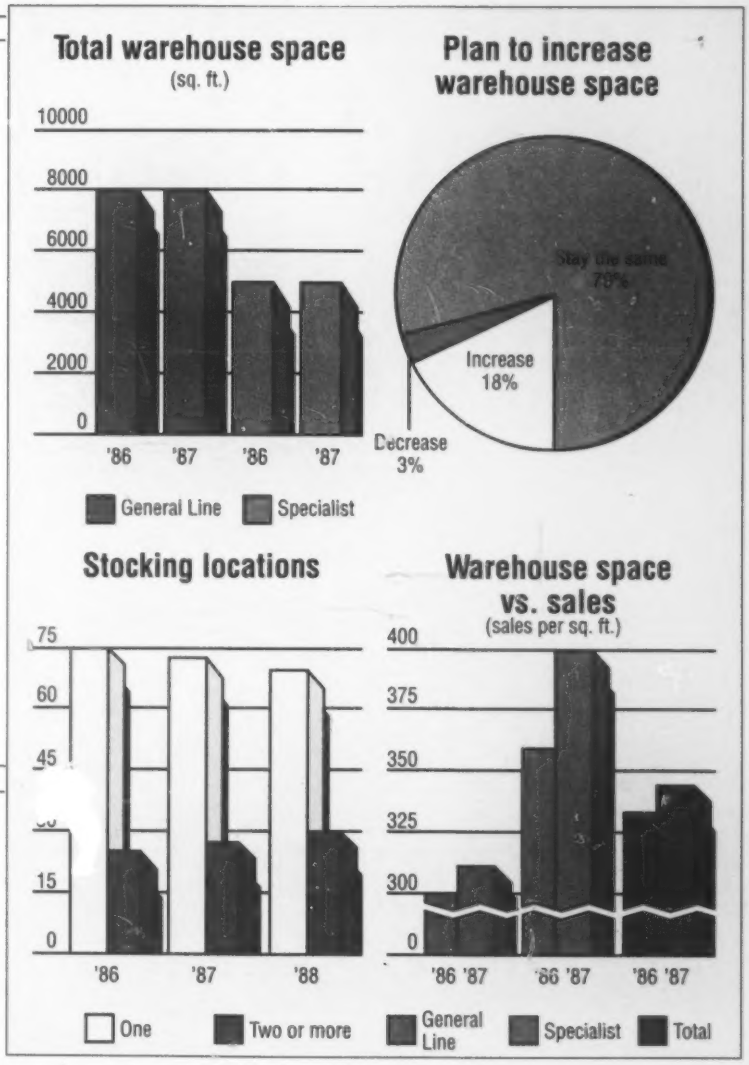
OPERATING COSTS

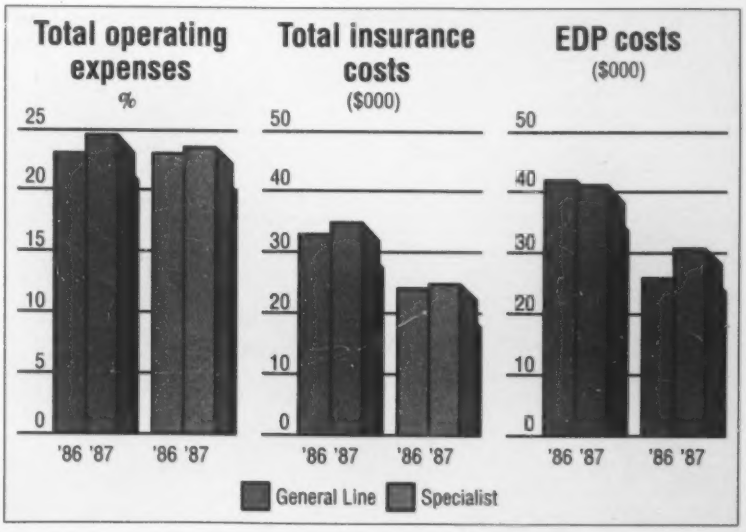
During the year, insurance and data processing costs increased. The average general line distributor paid $35,000 in premiums in 1987, versus $33,000 during 1986. In addition, 1 distributor in 10 was involved in a product liability suit, while nearly a third of those were penalized. The average "settlement" was $3,475.

Electronic data processing (EDP) costs rose sharply last year for specialty distributors, increasing an average of $5,000, or nearly 20%. While part of these higher costs are attributable to new equipment, specialists also paid more in salaries, perhaps reflecting increased wages as opposed to hiring of additional staff. In contrast, generalists spent slightly less on EDP in 1987 ($42,000 versus $41,000), with equipment expenditures being squeezed $1,000 from a previous budget of $11,000.

How to order

Complete copies of the 42nd Annual Survey of Distributor Operations are available in report form. For ordering information, see p.39.





Industrial distributors are computerized, and the way in which they conduct their businesses will never again be the same. In 1987, nearly three-quarters of all distributors surveyed used computers in some aspect of their business and, if the past is any indication, that figure is likely to increase.

More important than the overall "computerization" of the industry, however, is how well electronic data processing (EDP) is serving those who already use it.

Not only are computerized distributors enjoying sales three times greater than those of distributors using the "conventional" approach, but more importantly, they are far more profitable as well (see table above right).

A look at employee productivity levels reveals the advantages of EDP. Gross profitability is higher for businesses with computers, as are gross profits per employee. In addition, whereas each employee in a non-computerized distributorship accounts for $138,000 in sales, those with computers command sales of $180,000; a difference of 30%.

THE DIFFERENCE IS PROFITS

In perhaps the best measure of profitability, computerized distributors achieved ROI of 9%, compared to only 7% for those without computers. In creating a hypothetical sales model of two distributors with sales of $1 million each, the computerized distributor would have net profits after taxes of $21,040, while the "conventional" business would have nearly one-third less to take home, or just $16,370.

There were few surprises in the area of business automation. As the accompanying table indicates, the larger the distributor's sales, the greater the use of computers and facsimile machines, and the existence of electronic order entry capabilities.

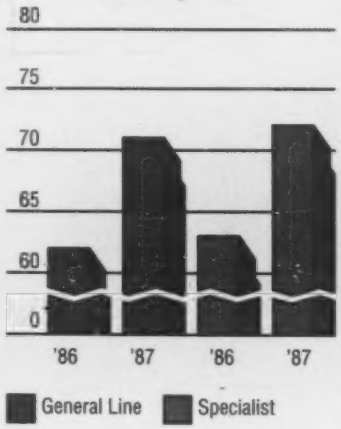
Beyond the information which clearly indicates the benefits of computers, there is perhaps another less obvious message being sent. While there are many non-computerized distributors making money, and perhaps even a lot of money, computerized distributors have a choice not available to their counterparts: that is the option to grow.

Indeed, the evidence is clear. Choosing to remain a small, profitable business without the advantage of a computer is, at best, a very large risk. But lacking automation dictates that a business must remain small.

How computerized and non-computerized distributors compare

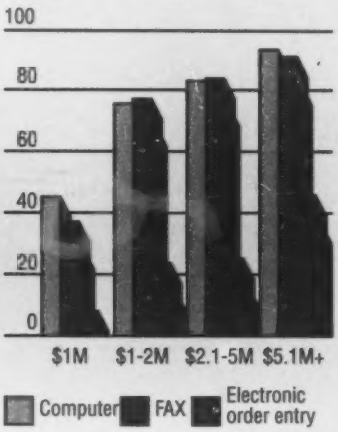
	Computerized	Non-computerized
Total sales ($000)	$2700	$825
Gross profits (% of total sales)	28%	24%
Actual gross profits ($000)	$756	$198
Gross profit per employee ($000)	$50.4	$33.0
Sales per employee ($000)	$180	$138
Return-on-investment (% of total net worth)	9%	7%

Percent using a computer



Business automation

distributors by sales ($ millions)



How to order the Survey

How do you stack up against the competition? Analyze and compare all aspects of your company performance with the *42nd Annual Survey of Distributor Operations*, available in report form. It contains over 300 pages of original statistics on general line, specialty and combination distributors. Comparisons of distributor performance by annual sales and five geographic regions are included. The *Survey* is the most complete reference of its kind in the industry. A single copy is $175 prepaid. Write: INDUSTRIAL DISTRIBUTION Annual Survey, Cahners Building, 275 Washington St., Newton, MA 02158, Attn: Diane Mercurio, or call (617) 558-4346.

Rate your company's performance

This table provides a brief but important overview of industrial distribution. Space is provided for your company's figures; please be careful to compare your numbers with the appropriate category.**

***General Liner:* No one product category contributes 50% or more to total sales.
Specialist: 50% or more of your total sales comes from one major product category, such as fasteners.

	General Line		Your Figures		Specialist	
	'86	'87	'86	'87	'86	'87
Total sales ($ millions)	2.4	2.5			1.8	2.0
Cost of goods sold (% of total sales)	73.0	71.0			70.0	70.0
Gross profit (% of total sales)	24	25			27	28
Total operating expenses (% of total sales)	23.0	24.5			23	23.5
Net profit before tax (% of total sales)	5.0	3.5			4.0	4.0
Net profit after tax (% of total sales)	3.0	2.0			2.0	3.0
ROI (return on net worth)	9.0	8.5			7.0	8.0
Sales per employee ($000)	218	208			180	200
Receivables value as of Dec. 31, '87 ($000)	232	260			200	250
Receivables outstanding (# of days)	42	41			45	45
No. of invoices billed yearly	5500	6000			3680	4000
Avg. # of items per invoice	4	5			4	4
Avg. invoice value ($) (sales divided by yearly invoices)	436	416			489	500
Sales per sq. ft. of warehouse space ($) (sales ÷ total warehouse space)	300	313			360	400
Total payroll ($000)	276	247			225	215
Payroll per employee ($000)	25	21			23	22

42ND ANNUAL SURVEY

Combination houses post 12% sales gain

Evidence mounts that distributors wholesaling their goods to non-industrial markets outperform their peers in profitability.

The nation's wholesale-industrial distributors, also known as combination houses, increased their sales 12% during 1987. For general line distributors in this category, average median sales rose a slim 3.3% in 1987 to $3.1 million. For specialists, the year proved far more successful, as sales jumped 25% to a median average level of $3 million.

But neither category of distributor could justifiably complain about year-end operating results. For the generalist, gross profits increased from 24% of total sales to 26%, and specialists followed suit having raised profitability from 23.2% in 1986 to 28.5% in 1987.

In comparing combination houses to the more "traditional" industrial distributor, it becomes apparent that the combination business is somewhat more profitable. Take, for example, return on investment (ROI) as a measure of profit as a percent of net worth. During 1987, combination houses averaged an ROI of 10% (9.0% for generalists and 8.5% for specialists).

For the distributor not engaged in wholesaling, industry ROI averaged only 8.0%, with generalists achieving an 8.5% return on net worth and specialty distributors obtaining an 8% return.

Why then were combination houses more profitable than industrial distributors last year? Unfortunately, a look at the goods sold by combination houses reveals too few answers. Last year, an increasing number of distributors sold plumbing and heating supplies, but based on sales in that industry, it's doubtful that increased profitability was accomplished there. In fact, Virginia-based Noland Co., which receives 59% of its sales from plumbing and heating, reported declining sales of 3% for that industry segment.

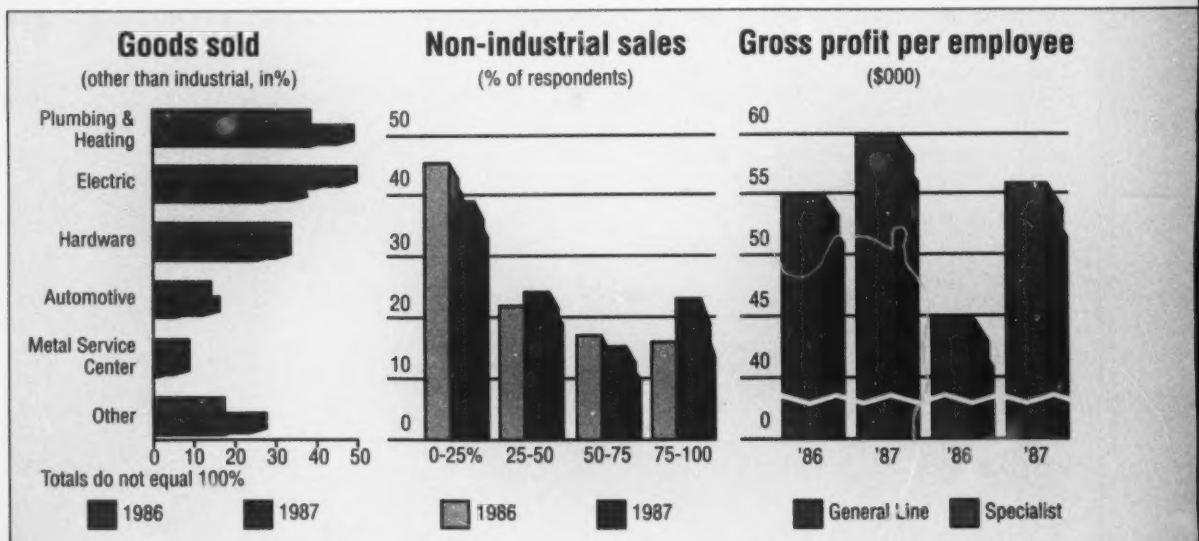
Gains, however, may have been made in the automotive aftermarket, where sales increased from 14 to 16%, as well as from a wide variety of "other" sources (see chart).

Gross profits per employee also improved for the year. Generalists managed to increase their workers' efficiency 11%, while specialists boosted employee output from $45,000 each to $56,000 per worker: an improvement of 25%.

On the receivables front, generalists reduced the value of their outstanding billings nearly 17%, from an average of $260,000 to $217,000. Specialists also fared well, reducing their receivables from $248,000 to only $200,000, a reduction of 19%. Some headway was lost, however, although not by much, in the number of days collections were outstanding. For both generalists and specialists, average billing was outstanding 45 days.

New to this year's survey were questions pertaining to management's view of profitability. As seen in the accompanying pie charts, 46% of general line distributors thought their businesses had become more profitable in the past 5 years, while only 32% of specialty distributors agreed with that assessment.

Although 1987 figures suggest



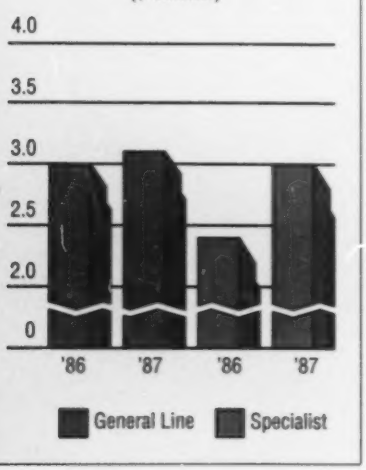
How to order

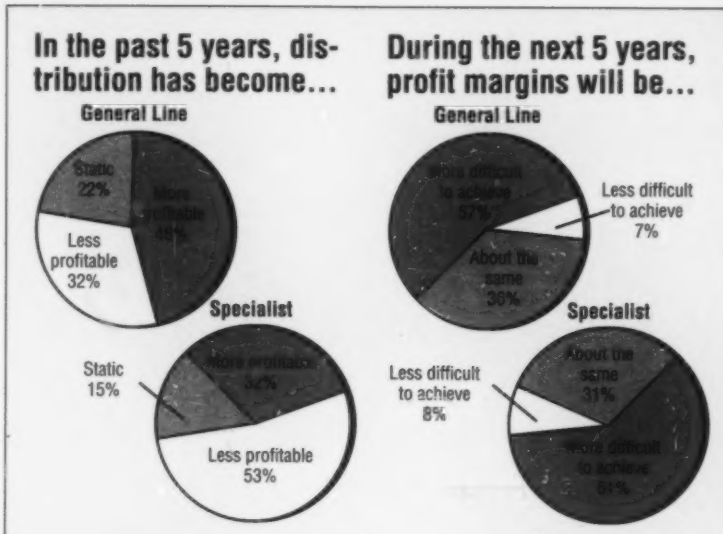
The *42nd Annual Survey of Distributor Operations* contains detailed information on industrial distributors selling to wholesale and non-industrial markets. It contains over 300 pages of original statistics on combination houses as well as general line and specialty distributors. Comparisons of distributor performance by annual sales and five geographic regions are included. A single copy is $175 prepaid. Write: INDUSTRIAL DISTRIBUTION Annual Survey, Cahners Building, 275 Washington St., Newton, MA 02158, Attn: Diane Mercurio, or call (617) 558-4346.

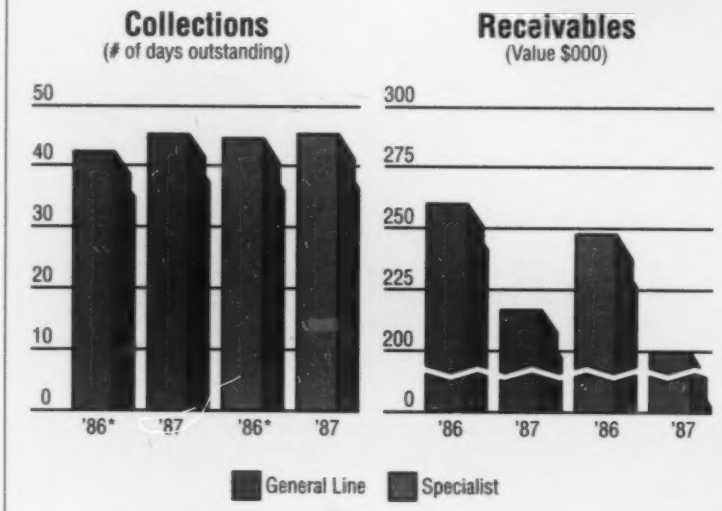
that generalists are less profitable than specialists, 32% of generalists and more than half of all specialists thought distribution had become less profitable.

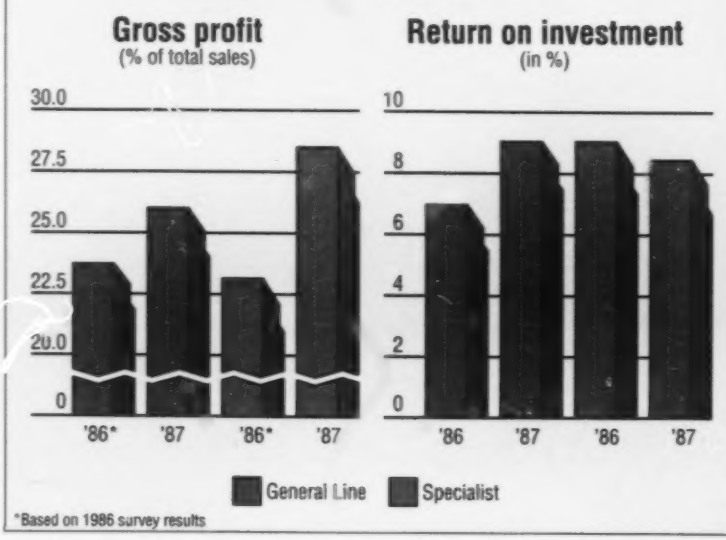
When questioned about the future, a majority of general line and specialty distributors (58%) believed profit margins would be more difficult to achieve during the next 5 years. In stark contrast, a mere 8% of the respondents thought profitability would be less difficult to achieve in years ahead.

Whatever the truth may be regarding profits, the 1987 *Survey* makes at least one point clear; last year, combination houses made more money than general line and specialty distributors. And if any distinctions are important in business, it's safe to assume that profitability counts. □









*Based on 1986 survey results

As OSHA regulations tighten and jury awards skyrocket, manufacturers and customers demand that safety distributors be experts.

Expertise drives SAFETY SALES

By Steve Zurier, Associate Editor

The story of the modern safety equipment supply industry dates back to the 1940s, when the United States geared up its industrial plant to meet the challenges of World War II. At that time, manpower was scarce and employee safety was considered a part of our national defense effort.

As enterprising Americans are apt to do, a business grew out of this initial demand for a safe workplace. Although some large general line distributors moved into the field, it was the specialized safety equipment distributors that were in the best position to meet the needs of industry when the federal government created OSHA in 1971.

Rick Tango

Product knowledge is critical today, says Industrial Safety Supply's Ralph Muszynski, who demonstrates how to operate a respirator.

Today, with a recent federal appeals court ruling which says that *all* companies must abide by OSHA's Hazard Communication Standard (see ID: April '88, p.25), the demand for expertise in the safety equipment field has never been greater.

Notes Jim Foster, public affairs director for OSHA, "It's clear that the firms which pay close attention to detail are the ones that will be successful during the 1990s."

One of the most obvious results of the upgraded OSHA standards is that safety equipment manufacturers are demanding that distributors be experts. For example, 3M's Occupational Health & Safety Products Div. (OH&SP) requires their distributors either to specialize in the field or have a division that deals specifically with safety equipment.

Says Robert Pereson, OH&SP's national sales manager, "Our distributors need to know not only the products, but the necessary training to use the products properly. We believe it's the professionals on staff within a distributorship who make the difference in the sales and service."

This emphasis on professionalism is what's made 3M distributor Vallen Safety Supply Co. of Houston, TX, one of the largest safety equipment distributors in the country. Founded in 1947 with one product line, Vallen now boasts sales in excess of $75 million with 24 operating branches in 11 states.

R.R. "Butch" Hutton, Vallen's president, notes that the large safety equipment distributorship has grown so successfully over the years due to the expertise of the employees the company recruits and trains, its extensive product line and the exceptional level of service it main-

tains in selling those products.

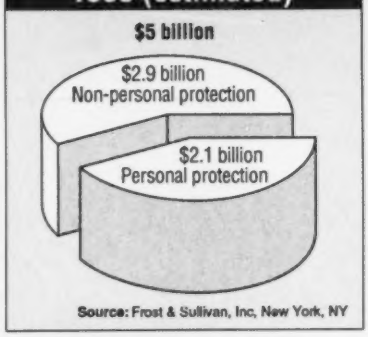
Vallen, certainly not restricted to carrying only 3M products, sells more than 10,000 specialized and commodity items from more than 250 manufacturers.

As part of its overall service package, Vallen offers repairs on respirators, fire extinguishers and portable instruments. If necessary, the company establishes on-site repair shops at the job site. While Hutton acknowledges that Vallen's core business is still in the chemical processing and oil refining industries, the firm has branched out over the years into the pulp and paper, electronics and food processing fields.

To meet special customer needs, Vallen works closely with suppliers to provide custom-engineered equipment. Some examples include a monitoring system for use in high noise areas, specially fabricated steel cabinets which protect remotely located respiratory equipment from bad weather and pilferage, and custom-built emergency respiratory trailers equipped to rush needed breathing apparatus to remote areas.

Says Hutton, "We can do anything the customer wants us to do, as long as it satisfies a need and provides a fair profit opportunity."

Safety Equipment Market 1988 (estimated)



Estimated at $5 billion in 1988, the safety equipment market will grow 4.3% annually through 1991.

'What I want my people to strive for is quality time with quality accounts.'—Muszynski

A SIMPLE SALES PHILOSOPHY

Vallen is an example of a large distributorship that grew by expanding both its product offerings and branch operations. Connecticut-based Industrial Safety Supply Co. has kept a New England market orientation, but has grown over the years by expanding its product mix.

Along with selling safety supplies, the firm, founded in 1945, now operates separate divisions for materials handling supplies; industrial plastic supplies and plastic fabrication, maintenance and medical supplies; and fire and rescue equipment. The firm does all of this out of its 165,000-square-foot facility in West Hartford.

Ralph Muszynski, Industrial's general manager and vice president, has a simple sales philosophy. Notes Muszynski, "The idea in selling safety equipment is to obtain sound product knowledge, acquire a broad based product line, learn about your customers, then develop the appropriate skills and expertise to get the job done."

As Muszynski explains, what he tries to instill in his field salespeople is the old axiom that 20% of their customers will account for 80% of the business they write up. "What I want my people to strive for is quality time with quality accounts. The salesperson has to get in front of the customers and see to it that they are exposed to as many of our product offerings as possible."

In Muszynksi's mind, most of selling is common sense. Says Muszynksi, "What I want is a guy who knows that during the winter, if he's selling industrial boots, thinks to ask if the customer needs rain gear, gloves, snow shovels, rock salt, or any number of ancillary products that can assist the customer and in-

Rick Iengo

Dependable repair work tailored to the needs of customers is an integral part of the sales strategy of most successful safety equipment distributors.

crease our margins. There's always a way to increase sales if the salesperson's alert."

THE MANUFACTURER'S ROLE

Distributors can also enhance their sales strategies by taking advantage of the services their manufacturer partners provide.

For example, Ross Giordano, director of marketing for Justrite Manufacturing Co., notes that his firm supports Industrial Safety Supply and other distributors by offering free product literature and catalogs, educational tapes, sales training seminars, and cooperative advertising.

The cooperative advertising program involves credits which Justrite passes back to the distributor for use as he sees fit. These credits are based on the amount of sales volume a distributor generates.

Notes Giordano, "We let our distributors make the decision. Some spend the money producing their own catalogs, while others advertise in local newspapers, start direct mail programs or hold open houses."

A SENSE OF THE MARKET

So with all of these specialized distributor services, selling philosophies and manufacturer support systems, you may ask, "What's the market like?"

The best market information available is a 391-page report published last year by Frost & Sullivan, Inc., a New York City-based research firm.

According to John B. Scott, the researcher on the project, the occupational safety equipment market will grow at an annual rate of 4.3% through 1991.

Scott estimates that for 1988, the market, defined as any product that ensures health and well-being in industrial plants and business offices, is expected to reach $5 billion dollars.

By dividing the market into two sections, personal and non-personal protection, Scott found that the personal protection market, which includes head, face, eye, ear, hand, foot, and respiratory protection equipment, would be worth $2.1 billion. The non-personal market, the bulk of which involves fire protection and air pollution equipment, is estimated at $2.9 billion (see chart).

Says Scott, "The fact of the matter is that it has become apparent to many firms that there is too much at stake economically, so companies must continue reducing the rate of fatalities, injuries and illnesses incurred on the job."

In this heavily regulated environment, distributors are bound to always have a core business they can depend on. But not just anybody can go into safety equipment sales. Whoever is interested must make a substantial investment in inventory and training and be prepared to compete against the combined purchasing power of the independents (see box) and the growing strength of the large distributors. □

We can do anything the customer wants us to do . . .' —Hutton

Selling safety as a group

When independent safety equipment distributors looked into the future, they saw a marketplace in which a few key players controlled a significant share of the business.

Enter the Safety Marketing Group.

Formed on Jan. 1, 1988, the Cincinnati, Ohio-based organization, also known by its acronymn SMG, is yet another effort by independents to gain competitive buying and selling advantage through the formation of a marketing group (ID: June '88, p.7).

Notes James R. Gardner, SMG's president, "In an industry that is being squeezed by highly capitalized firms, the independents find it tougher and tougher to maintain a healthy profit level. SMG is a concerted effort on the part of independents to remain competitive."

Based on a similar marketing group that Gardner manages for the paper industry, SMG has clearly caught on with independents. In a few short months, SMG has blossomed into a nationally based organization of 20 distributors, which combined represent more than $80 million in sales.

According to Gardner, one reason distributors find SMG attractive is that it lets them provide manufacturers with substantial volume and marketing services in exchange for a marketing allowance. This allowance is administered by SMG, but ultimately passed back to the distributor.

Some of the services SMG provides include yearly distributor/supplier meetings, monthly newsletters and a buyer's guide. SMG also offers closed product categories combined with the assurance that each distributor member will buy a minimum of 25% of their yearly purchases from SMG's preferred vendor list.

SMG is a concerted effort on the part of independents to remain competitive. —James R. Gardner

Robert Miller, national sales manager for The Protectoseal Co. of Bensenville, IL, maintains that SMG provides a fair trade-off.

Notes Miller, "We were already doing business with about 13 of SMG's members, so the advantage to us is that we were able to pick up a few more distributors and give the companies we've had longstanding relationships with more incentive to sell our product."

The incentives from the manufacturer translate into a real sales advantage, according to A.R. Dooley, Jr., chairman of Deer Park, Texas-based Dooley Tackaberry Inc. and secretary of SMG.

Says Dooley, "SMG gives the distributor the ability to sell a broad range of products that he can buy and resell at competitive prices. With this advantage, our members can better service their customers."

It's still too early to tell whether or not SMG will become a prominent player in the safety equipment field, but one fact is certain. The forming of SMG has sent a message to the marketplace that independents recognize the challenge before them and are ready to give larger distributors a tough fight.

BUSINESS REPORT

BY KRIS BLEDOWSKI

Prices kept in check

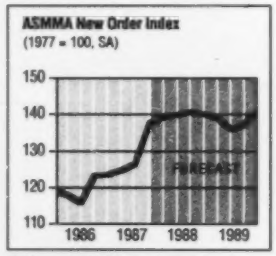
Labor productivity increasing sharply

Despite inflationary pressures in the American economy, many companies are holding back on price increases for finished goods. The economy was operating at 82.7% of capacity utilization in April, a rate that economists regard as "full employment" of resources. Such a high level of activity usually pushes prices for primary and intermediate materials up and bids up labor costs as well. The resulting tendency is for manufacturers to raise prices for finished products.

It appears that the moderate inflation for finished products is the result of competitive forces in the marketplace. Within the last 10 years, foreign suppliers forced American producers to check price increases by shipping more low-cost goods into the U.S. Flat domestic demand reinforced this trend. Manufacturers have partially offset higher input prices by increasing productivity and lowering profit margins.

A case in point is the paper industry. The cheap dollar stimulated foreign demand for pulp and paper. To meet the demand, paper mills pushed their capacity utilization to over 90%. As a result, prices for these products have risen 30% over the past 2 years. However, most companies have not passed along all the price increases.

Another reason the inflation rate has not risen sharply is that labor costs have been held down. As a result of capital investment in newer and more efficient technologies, labor productivity—an employee's output per hour of work—has increased markedly. It is expected, however, that wages will soon start rising as well. Some regions, notably the Northeast and Midwest, are already experiencing labor shortages. Higher wages will inevitably increase the labor component in total costs. How much more will companies be able to sacrifice profits by holding prices is unknown. □



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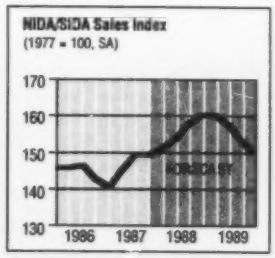

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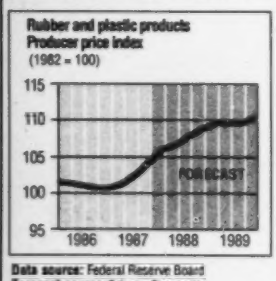

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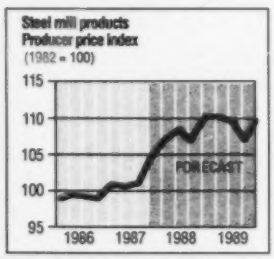

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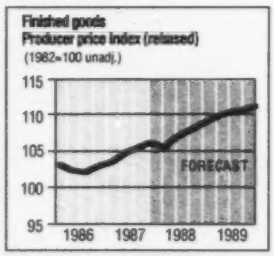


Data source: Federal Reserve Board
Forecast source: Cahners Economics

Data source: Federal Reserve Board
Forecast source: Cahners Economics

SALES BY REGIONS (% change)	SALES (%) March '88 vs. March '87			RECEIVABLES (# of days) Feb. '88 vs. Feb. 87						INVENTORIES		
	Gen.	Spec.	Comb.	Gen.	Spec.	Comb.	Gen.	Spec.	Comb.	Increase Levels	Remain The Same	Decrease Levels
NEW ENGLAND CT, RI, MA, NH, VT, ME	10	11	9	46	49	26	48	48	28	15	85	0
MID-ADLANTIC NY, NJ, PA	18	40	212	43	43	NA	41	44	NA	50	50	0
SOUTHEAST DE, DC, MD, VA, WV, GA, NC, SC, FL	24	–44	0	35	41	38	41	41	98	38	48	14
NORTH CENTRAL OH, IL, IN, MI, WI	3	4	0	32	49	43	32	52	38	35	53	12
SOUTH CENTRAL AL, MS, KY, TN	22	37	14	37	42	64	31	35	70	42	54	4
MIDWEST MN, ND, DS, IA, NE, KS, MO	55	14	80	62	36	50	68	41	48	50	45	5
SOUTHWEST AR, LA, OK, TX	–1	13	29	45	39	50	54	44	51	47	43	10
MOUNTAIN NM, AZ, CO, UT, NV, WY, MT, ID	3	10	–13	40	41	43	43	41	45	39	39	22
PACIFIC CA, OR, WA	16	21	35	31	35	48	33	35	49	48	42	10
U.S. TOTALS	11	21	3	39	42	47	43	42	47	42	49	9

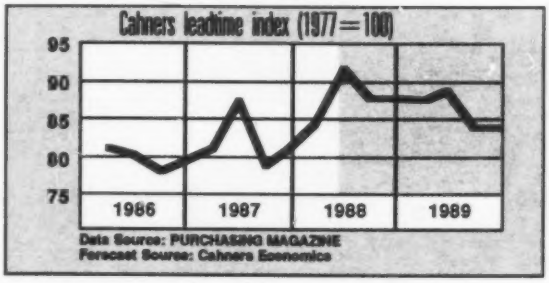
SUPPLY OUTLOOK

BY KRIS BLEDOWSKI

Economy at full employment

No recession seen through '88

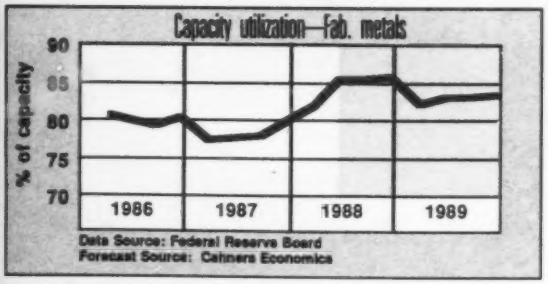
The economy shows no signs of slowing down. Capacity in all industries increased to 82.4% in the first quarter of this year, with primary processing leading the way at 86.8%; this is the highest level since 1979. The biggest strains were registered in the paper industry (95.5%) followed by textile mill products (90.8%), rubber and plastics products (88.6%), and aerospace (88.3%).



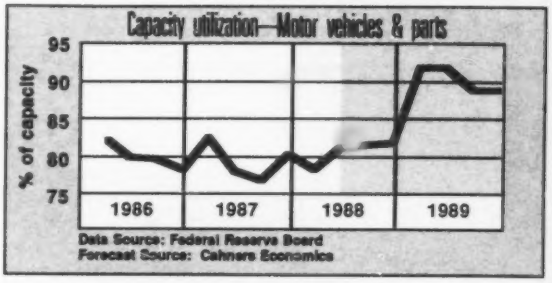
The strains are registered mostly in industries which have recently increased their exports. Operating rates for both electrical and nonelectrical machinery continued to rise throughout the first quarter, as did the rate for fabricated metal products. Aerospace industry is virtually export-led. Utilization at automobile assembly facilities also continued its rebound from very low rates at the start of the year. It is expected that motor vehicles, unlike other industries, will see high utilization ratios in 1989. Auto companies are trying to maximize their returns from modernized facilities, eliminating many plants altogether.

The Cahners Leadtime Index rose 3.3% in May after falling 2.3% in April. It was up 4.5% in the first quarter compared with the last quarter of 1987. The peak leadtimes will occur in the second quarter of this year when backlogs of orders from the booming first quarter will develop. For the year the index will be up 7.1%.

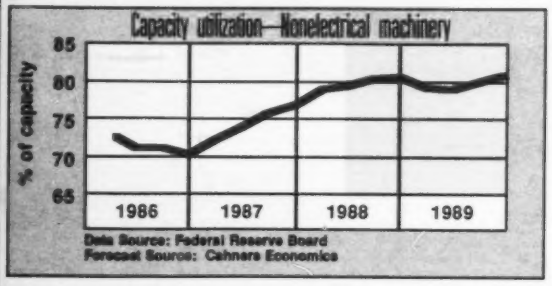
The economy should avoid the recession at least through the end of the year. The subsequent downturn will be shallow, with exports mitigating some of the domestic slack in aggregate demand. Foreign economies are expected to grow robustly through 1989, providing an outlet for American manufacturers who have invested billions of dollars in new technologies. This will result in continued improvement of the U.S. competitive position on world markets. □



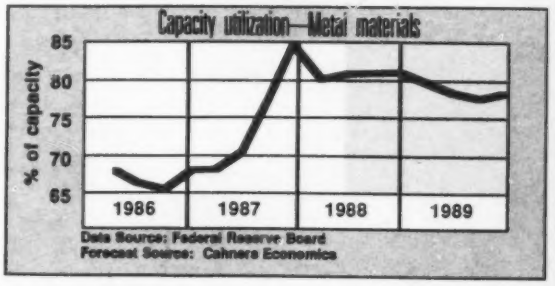
Capacity utilization of fabricated metals will stay high through the year due to high exports.



Auto companies are better utilizing existing facilities due to more capital-intensive technologies.



Exports of machinery accounted for the bulk of rising capacity that was reported.



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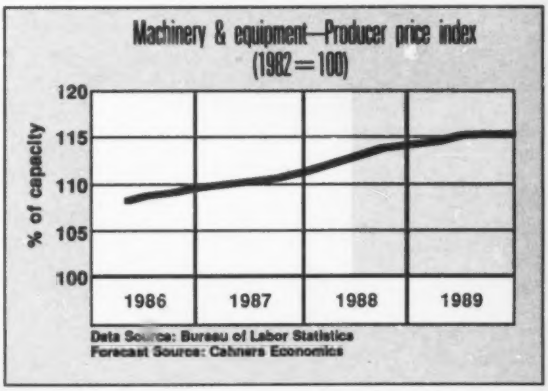
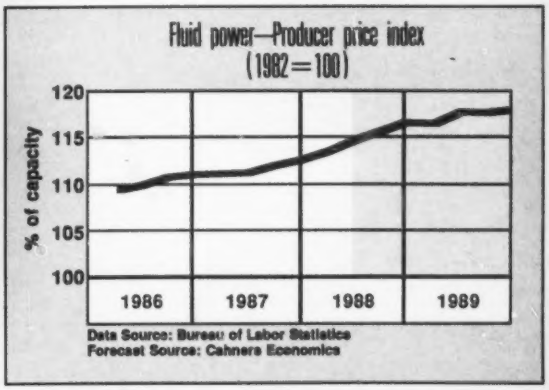
SUPPLY OUTLOOK

Capital equipment prices stable

Following a 0.4% increase in March, the Producer Price Index for capital equipment recorded a 0.2% rise in April. A downturn in motor vehicle prices was largely responsible for the slower April pace. Indexes for metal cutting machine tools and oil field and gas field machinery showed little or no change after substantial March increases. In contrast, prices for civilian aircraft, printing trades machinery, and pumps and compressors climbed considerably more than in March. This was due to tightening of supply conditions in these markets.



Producer prices of machinery rose 0.8% in the first quarter of 1988.



The Fluid power industry is booming but price increases should be moderate.

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